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February 21, 2012

To: Supervisor Zev Yaroslavsky, Chairman
Supervisor Gloria Molina
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Supervisor Michael D. Antonovich

From: William T Fujioka
Chief Executive Officer

SACRAMENTO UPDATE

This memorandum provides an analysis and a report on legislation of County interest related to the dissolution of redevelopment agencies which would have a significant impact to the County; and legislation to allow successor agencies to file for bankruptcy.

Redevelopment Legislation of County Interest

As previously reported, AB 1585 (Pérez), which was introduced on February 2, 2012, would make changes to ABX1 26 (Chapter 5, Statutes of 2011), to modify the provisions relating to: 1) the distribution of Low Moderate Income Housing (LMIH) funds; 2) the definition of the terms enforceable obligation and administrative cost allowance; 3) the responsibilities of the successor agency and oversight board; and 4) the responsibilities of the auditor-controller, among other provisions. The bill contains an urgency clause making it effective immediately, if passed by a two-thirds vote of the Legislature and signed by the Governor.

Background

ABX1 26 eliminates Redevelopment Agencies (RDAs) and provides for the transfer of property tax revenues to successor agencies, the retirement of RDA debts and for limited administrative costs. The remaining revenues are to be distributed as property

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taxes to cities, counties, school and community college districts and special districts. RDAs were dissolved on February 1, 2012.

Overview

Some provisions of AB 1585 are similar to those contained in **County-supported SB 654 (Steinberg)**, others are new. Significant differences are described below.

AB 1585 contains the following major provisions:

- **Transfer of LMIH Funds.** Like SB 654, AB 1585 would allow the local housing authority or the California Department of Housing and Community Development to retain LMIH funds if the city or county chooses not to assume the housing functions previously performed by an RDA.

In addition, AB 1585 specifies that if a city or county has not encumbered 80 percent of monies in the LMIH fund within three years of receiving the funds, the excess amount, minus the amount necessary for monitoring and maintaining ongoing housing projects, shall be allocated to the auditor-controller for existing housing purposes.

- **Expansion of the Enforceable Obligation Definition.** Like SB 654, AB 1585 would expand the definition of an enforceable obligation to include two additional types of loan agreements between an RDA and its host city or county: 1) a loan that was executed within two years of the date of the creation of a project area, if the loan is specific to that project area; and 2) a loan to fund the RDA's FY 2009-10 Supplemental Educational Revenue Augmentation Fund (SERAF) payment to schools.

In addition, AB 1585 would further expand the definition of an enforceable obligation to include: 1) other loan agreements between the RDA and the city and county if the oversight board finds that the loan was for a legitimate redevelopment purpose, had economic substance, and was based on reasonable repayment terms; and 2) payments for costs incurred to fulfill collective bargaining agreements for layoffs or terminations of city employees who performed work directly on behalf of the former RDA.

- **Expansion of the Administrative Cost Allowance.** ABX1 26 provides an administrative cost allowance for successor agencies of up to 5 percent of the property tax revenue allocated to the successor agency for FY 2011-12, and up to 3 percent annually thereafter, but not less than \$250,000 annually.

AB 1585 would expand the definition of the administrative cost allowance to specify that: 1) employee costs associated with work on specific project implementation activities, including, but not limited to, construction inspection, project management, or actual construction, shall be considered project-specific and are not administrative costs; and 2) the oversight board may approve temporary increases to the administrative cost allowance to carry out the requirements of an enforceable obligation, cover litigation costs, or to maintain and preserve the value of assets while in the possession of the successor agency.

- **Expansion of Successor Agencies and Oversight Board Responsibilities.** AB 1585 would authorize successor agencies, with oversight board approval, to enter into agreements to fund required payments under enforceable obligations that exceed the amount of property tax revenue available to the RDA during the payment period. AB 1585 also would require successor agencies to take inventory of all of their real property assets and report the results to the oversight board.
- **Expansion of Auditor-Controller Responsibilities.** AB 1585 would require the auditor-controller to reserve additional funds in the Redevelopment Property Tax Trust Fund at the time of the annual January 16th allocation, if necessary, to cover payments made in the second half of the calendar year that are in excess of amounts anticipated to be deposited from the allocation in May or June.

Potential County Impact

Transfer of the Low and Moderate Income Housing Funds

According to the January 31, 2012 Senate Floor analysis of SB 654, the retention of undesignated LMIH by host cities or counties will prevent the reallocation of approximately \$1.36 billion in unreserved LMIH funds to local governments and schools. The analysis notes that this amount could increase if it is later determined that amounts reported by RDAs as reserved are not enforceable obligations. The analysis indicates that to the extent that SB 654 prevents property tax revenues from flowing to schools following the dissolution of the RDAs, there would be a corresponding loss of State General Fund savings, which would otherwise offset the Proposition 98 guarantee to education. Assuming that 50 percent of this revenue would be allocated to schools, the Senate analysis estimates a one-time State General Fund loss of as much as \$700.0 million. The remaining \$700.0 million in property tax revenue would no longer be available for reallocation to counties, cities, or special districts. **Since the LMIH**

provisions in SB 654 are the same in AB 1585, these fiscal impact assumptions would also apply.

According to the FY 2009-10 California Redevelopment Agencies Report issued by California Department of Housing and Community Development as of June 30, 2010, RDAs in Los Angeles County had unencumbered/undesignated balances in their LMIH Fund of approximately \$233.0 million. **Pursuant to the RDA dissolution provisions in ABX1 26 of 2011, these funds are to be distributed to taxing entities, including the County General Fund which may potentially be entitled to \$70.0 million to \$93.0 million (30 percent to 40 percent) of undesignated LMIH funds.** It is very difficult to determine the potential amount of LMIH funds which could be reallocated to the County, because the only data available at this time is from FY 2009-10 and the type of financial obligations RDAs may have entered into prior to their dissolution on February 1, 2012 is unknown.

County Counsel indicates that should unencumbered LMIH fund balances not be transferred to the auditor-controller for allocation as property tax revenue local taxing entities would be negatively impacted. County Counsel further indicates that absent this proposed amendment in AB 1585 the County would receive its proportionate share of property tax revenue.

County Counsel further notes that provisions which specify that if a city or county has not encumbered 80 percent of monies in the LMIH Fund within three years, the excess amount would be allocated to the auditor-controller for housing purposes, AB 1585 does not clearly indicate what the auditor-controller is required to do with these funds.

The Community Development Commission (CDC) indicates that under the provisions of AB 1585, it would be entitled to retain its share of undesignated LMIH funds by transferring them to Housing Authority for the County of Los Angeles (HACoLA). According to the CDC, approximately \$150,000 in non-encumbered CDC LMIH funds would go to HACoLA instead of being returned to other taxing entities, such as school districts, County General Fund, special districts.

Expansion of the Enforceable Obligation Definition

Expanding the scope of what is deemed to be an enforceable obligation, beyond that which is provided in ABX1 26, would reduce the total amount of tax increment that would otherwise be returned to taxing entities, such as the County.

County Counsel indicates that should enforceable obligations be expanded to include loans from host cities or counties to their former RDAs in the first two years after a new

project area was started, as proposed in AB 1585, local taxing entities, including the County, would be negatively impacted. AB 1585 also would treat any amounts a host city or county lent to their RDA to make SERAF payments as an enforceable obligation, which would also reduce the County's share of property tax revenue under ABX1 26.

It is difficult to estimate the fiscal impact from the expansion of the enforceable obligation definition would impact the County. The extent of the impact would depend on loan agreements executed on RDA projects within the two year period, as proposed in AB 1585. While we have found some preliminary examples within the County where this provision would apply, most of this information would not be available to county auditor-controllers and successor agencies until months after the dissolution of RDAs when all audits have been completed.

Based on a preliminary analysis of Auditor-Controller data provided by redevelopment agencies, it is estimated that there is roughly \$856.0 million (principal and interest) of existing loan agreements between RDAs and host cities or counties. By analyzing a sample of existing agreements between RDAs and host cities, it was determined that an estimated 10 percent of those contractual obligations would qualify as "additional enforceable obligations" pursuant to the provisions of AB 1585. **Therefore, it is estimated that the expansion of the enforceable obligation definition under AB 1585 could result in the potential loss of \$85.0 million for taxing agencies within Los Angeles County, of which the County General Fund could lose approximately \$34.0 million.**

Furthermore, AB 1585, unlike SB 654, also proposes to consider additional loans between a host city or county and a former RDA as enforceable obligations, if an oversight board makes a finding that the loan was for a legitimate redevelopment purpose, had economic substance and was based on reasonable payment terms. It is difficult to estimate the impact of this amendment because it is nearly impossible to know which loans would meet the criteria and whether oversight boards would exercise their discretion to treat the loans as enforceable obligations. In addition, a major concern of the Chief Executive Office, County Counsel and the Auditor-Controller has been the potential for a number of RDAs that had been actively issuing debt during 2011. According to County Counsel, even if only one such loan is treated as an enforceable obligation it will result in less property tax revenue for local taxing entities.

County Counsel indicates that the impact of expanding the definition of enforceable obligation to include the costs to fulfill collective bargaining agreements for city employees who perform work for the former RDAs is unclear at this time. However, under current law collective bargaining Memorandums of Understanding are considered enforceable obligations. The Auditor-Controller indicates that this provision could

eliminate protections under current law, which may be interpreted to define the set of agreements deemed an enforceable obligation.

Expansion of Administrative Cost Allowance

County Counsel indicates that any increase in the administrative cost allowance would potentially result in a negative impact to the County because it would reduce property tax allocations to all local taxing entities, including the County. Further, by specifying that certain employee costs would be considered project-specific and not administrative costs, County Counsel indicates that this would allow successor agencies to collect more property tax increment by avoiding having to include employee costs in the administrative cost allowance.

The Auditor-Controller indicates that the provisions expanding the administrative cost allowance are too broad and could lead to abuses by successor agencies, and that provisions related to employee costs could eliminate administrative cost allowance limits established in ABX1 26.

Overall the expansion of administrative cost allowance would result in a significant diversion of property taxes away from local governments.

Expansion of Successor Agencies and Oversight Board Responsibilities

County Counsel indicates that allowing successor agencies to enter into agreements to fund enforceable obligation payments that exceed the amount of property tax revenue could address cash flow problems; however, this provision would seemingly open the door to masking revenue problems.

With regard to requiring successor agencies to take an inventory of all of their real property assets, County Counsel notes that this provision would benefit the auditor-controller in performing audits of former RDAs and the Auditor-Controller concurs.

Expansion of Auditor-Controller Responsibilities

The Auditor-Controller indicates that provisions which would require funds to be placed in reserve to cover payments made in the second half of the calendar year that are in excess of amounts anticipated to be deposited from the allocation in May or June would be beneficial to the successful implementation of ABX1 26.

Conclusion

This analysis contains preliminary estimates, which may not be completely reliable because they are derived from limited information available and without the County having access to source documentation to verify its validity.

While the County has Board-approved policies to advocate on redevelopment legislation which would cause the County to lose revenues, we also have policies to support proposals that provide incentives to local governments and developers to increase and protect affordable housing and allow flexibility for counties to promote a diversity of affordable house types through local policies. In addition, on January 31, 2012, your Board adopted a motion to support SB 654.

Though AB 1585 is similar to SB 654, allowing for the retention of LMIH funds by a local housing authority, it would further expand the definition of enforceable obligations to include additional loan agreements approved an oversight board and certain bargaining agreements as qualified debt. Furthermore, AB 1585 would expand the administrative cost allowance and responsibilities for successor agencies and oversight boards, which may result in the diversion of property tax revenues away from local taxing entities.

This office, the Auditor-Controller, County Counsel, and CDC will continue to analyze the provisions of AB 1585 to determine potential County impact and will work on recommendations for consideration by your Board.

AB 1585 is currently at the Assembly Desk awaiting referral to a policy committee. Registered support or opposition is currently unknown. This measure cannot be set for a committee hearing prior to March 4, 2012.

Legislation of County Interest

AB 1692 (Wieckowski), which as introduced on February 15, 2012, would authorize a successor agency to a former RDA to file for bankruptcy under applicable Federal bankruptcy law.

ABX1 26 eliminates RDAs and provides for the transfer of property tax revenues to successor agencies, the retirement of RDA debts and for limited administrative costs. Successor agencies would typically be a city, county, or the city and county which established the RDA. These successor agencies are required to make payments for enforceable obligations and to principally wind up the affairs of the former RDAs. The remaining revenues are to be distributed as property taxes to cities, counties, school and community college districts and special districts. The restrictions on RDA

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operations are intended to preserve the revenues and assets of RDAs in order that those resources not needed to pay enforceable obligations may be available for use by local governments to fund core governmental services.

Current law also authorizes a local public entity, as defined, to file a petition and exercise powers pursuant to applicable Federal bankruptcy law, subject to specified procedures, including participation in a neutral evaluation process with interested parties or upon a declaration of fiscal emergency, as specified.

AB 1692 would expand the definition of a local public entity to include a successor agency and would allow a successor agency to file for bankruptcy subject to procedures under existing Federal law.

The Chief Executive Office, Auditor-Controller, County Counsel, and the Community Development Commission are reviewing AB 1692 to determine possible impact to the County.

AB 1692 is currently at the Assembly Desk. This measure may be heard in committee on or after March 17, 2012. There is no registered support or opposition on file.

We will continue to keep you advised.

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